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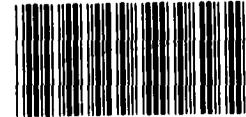
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CEO
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COMMUNITY AND ECONOMIC
DEVELOPMENT DIVISION

APR 8 1982

Mr. Philip Abrams
General Deputy Assistant Secretary
for Housing - Federal Housing
Commissioner
Department of Housing and Urban Development



119780

Dear Mr. Abrams:

Subject: (Review of the adequacy of procedures followed
in selecting Section 8 developers)

Our review of procedures followed by three Department of Housing and Urban Development (HUD) area offices (Atlanta, Chicago, and New York) in selecting section 8 developers for new construction and substantial rehabilitation projects disclosed some shortcomings and raised doubts at two of the offices concerning whether the best proposals had been selected in all cases. We found that

- proposals of competing developers had sometimes not been properly ranked,
- developers were selected without evidence that they had a legal right to the proposed building site(s)(site control),
- proposals from developers that were not selected were destroyed prematurely,
- preliminary evaluation meetings were not held to evaluate proposals.

We are recommending that appropriate corrective action be taken to ensure that all developers' proposals are promptly and adequately evaluated and that the basis for selection is fully documented in accordance with HUD's prescribed regulations and procedures.

The Section 8 Lower-Income Rental Assistance Program administered by HUD was established by the Housing and Community Development Act of 1974 (Public Law 93-383) and is the Nation's largest and most costly housing assistance program. Under this program, HUD selects developers to construct new housing and rehabilitate existing housing which the developers subsequently rent to eligible households.

HUD area offices initiate the new construction and rehabilitation programs by publishing Notifications of Fund Availability (NOFA) in newspapers of general circulation. NOFAs provide information to developers on the (1) amount of funding, or "contract authority," available for new or rehabilitated housing units, (2) number, location, and types of housing units to be constructed or rehabilitated, and (3) deadline for receipt of proposals. NOFA requests proposals from developers that are interested in providing the required housing. Both nonprofit and profit-motivated developers, alone or together with public housing agencies, may submit preliminary proposals in response to HUD's NOFAs.

Developers' preliminary proposals are required to include or indicate such information as (1) identification of the proposed building site, including a map showing site location and racial composition of the neighborhood, sketch of site plan, dimensions, unusual site features, and zoning, (2) documentary evidence that the owner has title to, or control of the site, (3) description of the proposed housing, including number and type of structures, (4) the contract rent per unit, equipment included in the contract rent, and utilities included and not included in the rent, (5) evidence that the proposed housing meets the local housing assistance plan, (6) evidence that proposed construction is permissible under applicable zoning ordinances or regulations, and (7) proposed method of financing and evidence that financing would likely be available.

Regulations covering submitting and processing section 8 project proposals are contained in 24 CFR 880, covering new construction, and in 24 CFR 881, covering substantial rehabilitation. In addition, HUD guidelines implementing these regulations which were to be followed in processing proposals in fiscal year 1979 are contained in HUD Handbooks 7420.1, April 1975, as revised through May 1978, which covers processing of proposals for new construction and 7420.2, June 1977, which covers processing of proposals for substantial rehabilitation.

HUD's area offices are responsible for reviewing all proposals received and for selecting those proposals which in total approximate the number of housing units called for in NOFA. The area office manager is responsible for overall direction of the section 8 program within the area office's jurisdiction and for assuring that that the processing is carried out in accordance with program regulations and the instructions in the HUD processing handbooks. The manager is assisted by several key area office personnel in the Housing Division, including the Housing Division Director, who are responsible for the program's day-to-day administration. Included are the Deputy Director for Multifamily Development who is responsible to the Housing Division Director for coordinating section 8 processing and cost, valuation, mortgage credit, and architectural and engineering technical processing

of proposals. The Deputy Director for Multifamily Development is assisted in these functions by the Chief of the Multifamily Housing Programs Branch and various staff members in the branch, including one or more multifamily housing representatives who are the focal points for coordinating section 8 proposal processing within the area office.

In addition, the Multifamily Housing Programs Branch obtains assistance in processing proposals from several other branches in the Housing Division, including the Valuation Cost and Architectural and Engineering Branches, which provide input to the multifamily housing representative on various aspects of the proposals.

OBJECTIVES, SCOPE, AND METHODOLOGY

We reviewed records, instructions, guidelines, regulations, and laws governing selection of housing developers in the section 8 program. We made our review at HUD's area offices in Atlanta, Georgia; Chicago, Illinois; and New York, New York. We also visited HUD's regional offices located in those three cities and its headquarters office in Washington, D.C., to obtain overall general information on the section 8 program and other pertinent information.

We made this review to evaluate the effectiveness of the procedures HUD follows to select developers to construct new housing and to substantially rehabilitate existing housing under the section 8 housing program. By directing our attention to the selection process, we sought to identify ways to improve the selection process and thereby possibly reducing housing costs and expediting completion of needed housing.

Our review generally covered proposals received for HUD's fiscal year 1979 requirements.

In Atlanta we randomly selected 20 of 174, or 11 percent, of all proposals received during the allowable time period to determine the timeliness and adequacy of preliminary proposal processing.

In New York we randomly selected a sample of 20 of 79, or 25 percent, of the proposals received that were approved.

In Chicago we selected 22 of 55, or 40 percent, of all applicable proposals approved. We selected the 22 proposals because they had lengthy processing periods and to expedite our identifying the obstacles delaying proposal processing and start of construction.

Our review was made in accordance with our current "Standards for Audit of Government Organizations, Programs, Activities, and Functions."

The shortcomings we observed at each area office are discussed below.

ATLANTA AREA OFFICE

Preliminary evaluation meetings
not held to evaluate proposals

The Atlanta area office did not hold preliminary evaluation meetings within the time or in the manner required by HUD handbook processing guidelines to determine whether preliminary proposals were ready for further processing.

HUD Handbook 7420.1, paragraph 3-6a, requires that the multifamily housing representative schedule a preliminary evaluation meeting within 5 working days of receipt of each proposal with other area office representatives from the Valuation and Architecture and Engineering Branches and the Equal Opportunity and Housing Management Divisions to accomplish specific review tasks and to determine whether the proposals are ready to be sent to the several area office branches and divisions for further detailed review of technical processing. A single session is to be scheduled when a substantial number of proposals are received. Further, paragraph 3-6c of the same handbook requires the multifamily housing representative to maintain a record of the results of each preliminary evaluation meeting and of the recommendations of each office's representative for acceptance, modification, or rejection of the proposal.

During our review of a random selection of 20 preliminary proposals, we saw no evidence that meetings were scheduled to make the required preliminary evaluation of proposals, or that proposals were evaluated on a preliminary basis by representatives of the specified area office branches. Instead, the evaluations were made by two multifamily housing representatives when they found time. As a result, the technical branches did not have a voice in determining whether the proposals were complete and ready for processing, as required by paragraphs 3-6a and 3-6c of HUD Handbook 7420.1. This appeared to us to have the potential for compromising the review process.

According to the responsible section 8 multifamily housing representative, the meetings had not been held because the area office received such a large number of proposals on or near the end of each month that they were unable to perform the evaluations as prescribed by guidelines with the insufficient staff available. Consequently, he and one other multifamily housing representative, who assisted in some section 8 program functions, performed the preliminary evaluations, whenever they were able to get around to them, to determine whether the proposals were complete. Afterwards, rejection letters were sent to developers of unacceptable proposals based on deficiencies noted by the multifamily housing representatives. Otherwise the proposals were found eligible for technical processing. The

section 8 multifamily housing representative also said that if the workload had been spread over a reasonable time frame, the area office would have had sufficient staff to preliminarily evaluate proposals in accordance with the handbook and the workload factor would not have been a problem. The required record of evaluation meetings was not maintained since no other review branch was involved in the review process. The same representative said that the area office was presently performing preliminary evaluations in accordance with the handbook.

The Director of Housing agreed that the review process could be compromised by not holding the preliminary evaluation meetings in accordance with the handbook.

NEW YORK AREA OFFICE

Proposals of competing developers not ranked prior to selection

Proposals received in response to fiscal year 1979 NOFAs were not ranked prior to selection as required by HUD Handbook 7420.1, covering new construction, and 7420.2, covering substantial rehabilitation. Instead, they were selected during meetings held by area office officials to decide which proposals would be approved and which projects would be rejected, and no record was kept on the basis for selection. As a result, there was no documentary evidence that the best proposals were selected.

Appendix 6, page 1, to both HUD Handbook 7420.1, change dated November 1976, and HUD handbook 7420.2, change dated June 1977, states that when available funding is insufficient to cover all approvable preliminary proposals, the approvable proposals must be ranked in order to select those which best meet HUD's requirements. Appendix 6, page 1 of both of these handbooks further states that each approvable proposal must be assigned a numerical rating, or score, based on its merits relative to the merits of other proposals within its group based on specific rating criteria. The criteria included proposed rents, site and neighborhood, design or rehabilitation concept, previous experience of the owner and other key participants in development and management, terms, conditions and likelihood of financing, overall feasibility, and comments on the project from local and State government units, regional, and metropolitan planning and developmental clearinghouses in accordance with Office of Management and Budget Circular A-95. The clearinghouses provide any comments which they may have, including observations concerning the consistency of the proposed project with State and areawide development plans, the extent to which the proposed project will provide housing opportunities for all segments of the community, and identification of major environmental concerns. According to the instructions, numerical values are assigned for each criterion: 5 points for excellent, 3 for good, and 1 for fair. Values assigned to each proposal are added and the proposals are put into rank order.

The highest ranked proposals meeting the required conditions in NOFA are supposed to be selected. This ranking and selection process was to be documented. Specifically, HUD Handbook 7420.1 paragraph 3-10c(2) requires that after the proposals are ranked, the multifamily housing representative shall transmit the proposals recommended for selection to the Housing Division Director for review, who then submits them to the area office manager for approval. The submission shall be accompanied by a memorandum, rating sheets, or other similar written documentation explaining the basis for the ranking and recommended selections.

The Deputy Director for Multifamily Housing Development in the New York area office said that the office had not complied in 1979 with HUD regulations requiring ranking but had ranked the proposals received in 1980. She said when she began work at the area office at the end of fiscal year 1977 proposals were not being ranked. In fiscal year 1978, she said, there was no NOFA, and in 1979 the office followed the same system it had used in 1977 when proposals were not ranked. She said decisions were made at meetings at the area office concerning which projects would be approved or rejected when proposals exceeded available funding. She also said the area office officials who attended the meetings kept rough notes, but HUD's requirement to document these meetings was never fulfilled.

We found evidence that the area office was ranking proposals in 1980, but we were unable to find any rough notes on the 1979 selections. Although the HUD area office reportedly followed the selection system used in 1977 when proposals were not ranked, we noted that HUD Handbooks 7420.1 and 7420.2 had also required that ranking be accomplished in fiscal year 1977.

The New York area office's failure to follow HUD Handbook 7420.1 and 7420.2 requirements that proposals be ranked and that the basis for ranking and selection be documented made it impossible for us to determine whether the best proposals were selected. There were, in fact, some indications that the best proposals may not have been selected. For example, 11 of the 20 proposals in our review received less than superior preliminary evaluations but were funded anyway. However, New York area office files showed at least six superior proposals were not funded because funding ran out and seven other superior proposals also were not funded, but the files did not show the reasons why.

The Deputy Director for the Multifamily Housing Division said that while lack of documentation makes it impossible to determine if the best proposals were selected, the proposals did undergo informal ranking, and that following HUD Handbooks 7420.1 and 7420.2, cited previously, regarding ranking and documentation of selections would not have changed which proposals were selected.

Premature disposal of preliminary proposals

The New York area office prematurely destroyed about 60 fiscal year 1979 preliminary proposals that had not been approved for funding. This improper destruction of official proposal records prevented any postaudit determination of whether the best proposals were selected and raised serious questions about the integrity of the proposal selection process.

HUD Handbook 2225.6, change 8, appendix 35, May 1980, requires that disapproved preliminary proposals for new construction and rehabilitation will be retained for 3 years after disapproval. Despite this requirement, the New York area office, on November 22, 1980, disposed of 60 of about 240 preliminary proposals received in response to fiscal year 1979 NOFAs. These proposals were less than 2 years old at the time of disposal. The 60 proposals had been rated "B" or "C" during preliminary evaluation and were not funded. A rating of "B" meant that judgment was being reserved on the proposal and it might be reconsidered in the future, and "C" meant the proposal was unacceptable. Proposals given an "A" rating are considered superior. We noted that 27 of the 60 discarded proposals were rated "B" the same rating given to 11 of the proposals we reviewed that were approved for funding. The other 33 disposed of proposals were rated "C" or unacceptable.

According to the Chief, Multifamily Housing Branch, the proposals were disposed of because there was insufficient room to store them. The official said they disposed of the proposals in accordance with HUD handbook 2225.6, appendix 1, item 3a. This section of the handbook, however, deals with mortgage insurance program files, not section 8 housing.

The Deputy Director, Multifamily Housing Division, told us that the basic reason for eliminating the files was lack of office space. She said she accepted full responsibility for disposing of the proposals and would do it again except for the fact that she now realizes that it would destroy an important part of the Division's audit trail.

Lack of site control

Eight of 20 preliminary proposals which we reviewed at the New York area office were approved without evidence that the developers had a legal right to the property proposed for development (site control). Further, on seven of the proposals which involved city-owned property, resolution of site control was delayed by a complex city review process and by untimely developer submission of proposals to the city for review. These factors contributed to delays in starting work and increased costs of some projects.

HUD regulations (24 CFR 880.305 (b) and 24 CFR 881.305 (b)) require that each preliminary proposal shall include or indicate documentary evidence that the owner has title to the site. The proposal may also include a copy of a contract of sale with respect to the site, or a copy of the site option agreement(s) or other legal commitment for the site. Based on these regulations, proposals should not be placed in processing or approved without documentary evidence of a valid option or sales contract. The regulations further provide that if the proposal is incomplete or deficient, the owner shall be advised in writing of the deficiencies and that the proposal is being rejected or that amendments or modifications will be accepted by a specified date.

Notwithstanding HUD regulations, section 8 developers that want to purchase New York City-owned property must also submit their proposals to a municipal process mandated by New York City's charter known as the Uniform Land Use Review Procedure (ULURP). This multistep process ordinarily takes about 7 months or longer to complete and should be initiated when developers are notified that their preliminary proposals have been selected.

We found that the New York Office had approved seven preliminary proposals for which the developers had not obtained title or other legal commitment from the city of New York to allow them to build or rehabilitate housing on sites owned by the city. Further, developers did not submit proposals to the city in a timely manner for review under the ULURP process after HUD had approved the preliminary proposals. Although HUD's project files did not show when the developers actually initiated ULURP processing, there was information in the files of five of the seven projects which indicated that ULURP processing had not begun before at least 3 to 9 months after preliminary proposals were approved.

For example, the area office approved one preliminary proposal (NY 36-0015-008) on May 30, 1979, without evidence of site control, then approved the final proposal on September 17, 1979, subject to the condition that the developer submit evidence that the city intended to convey title to the developer. However, the area office found no evidence at that time that the developer had initiated the ULURP process. One year later, on June 4, 1980, the developer said he had not obtained evidence of site control from the city due to delays in the ULURP process. He told HUD that the project, which was to have started in March 1980, would probably not commence sooner than August 1980. In addition, he requested more rental subsidy funds to cover increased costs caused by the delay. Later, in September 1980, after the developer obtained site control, the area office authorized rehabilitation to start, and as requested by the developer, increased the amount of funding reserved from \$615,480 to \$677,724 to cover the first year's rental subsidy.

We also found another proposal (NY 36-0015-077) where the New York area office had not verified whether the developer had site control even when city-owned property was not involved. Specifically, the area office approved the preliminary proposal but later learned that the developer had included in his proposal plans to substantially rehabilitate buildings which he did not own. After the legal owner of the property made this fact known, the developer withdrew these buildings from his proposal. This also delayed the production of needed housing.

Area office officials told to us that they were approving proposals before developers had site control. According to the Chief, Multifamily Housing Programs Branch, the multifamily housing representatives routinely indicated that developers had site control during preliminary review of proposals whenever city-owned property was involved. They said they approved the proposals under the assumption that New York City would eventually sell the property to the developers. According to this same HUD official, it was not practical for developers to begin the ULURP process until after the preliminary proposal was approved because developers are not willing to assume the expense of putting together detailed architectural sketches until they are assured that their proposal will be approved and funded. Likewise, New York City officials are reluctant to review proposed projects requiring ULURP unless they are certain that the proposal will be funded.

The Chief, Multifamily Housing Programs Branch, also said the area office generally approves final proposals before the entire ULURP process is completed. Also, in order not to delay the final approval process, it accepts a certification from the city planning commission to the local planning board on the developer's proposal as sufficient evidence that the developer will eventually get the site, in order not to delay the final approval process. But, she said, construction could not begin until the sale of the property had been approved by the city during ULURP.

The area office counsel told us that if the city planning commission has not provided certification to the local planning board, HUD will approve the final proposal conditionally, subject to receiving evidence of site control. This policy was initiated, according to the Deputy Director for Multifamily Development, so that the area office would not have to wait for the ULURP process to be completed while final proposals were otherwise ready for approval. She also said, that in the past, the area office realized that ULURP procedures were contributing to delays in proposal processing. Accordingly, in early 1980 the area office initiated a policy not to accept final proposal applications without evidence that ULURP proceedings had begun. The official said that this policy was instituted to improve coordination between the area office and New York City's ULURP process and to reduce the time required to approve final proposals.

CONCLUSIONS

The deficiencies we observed at the Atlanta and New York area offices indicated to us that the staffs in those offices did not adequately appreciate the importance of the proposal evaluation process. The extremely high cost to the Government of the section 8 program and the critical need for the housing units this program supplies requires that every reasonable effort be made to select the very best proposals available and to thereafter move expeditiously to construction. It is extremely difficult in the absence of relevant records and documentation to assess all the implications and effects of choosing less than the best proposals, although they might be expected to include: higher costs and rents to the Government than necessary, undue delays in getting construction started and completed, and fewer units being built or rehabilitated.

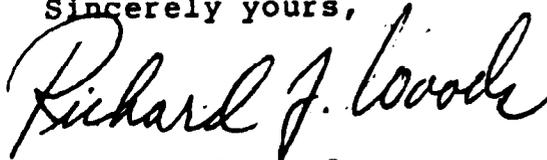
RECOMMENDATIONS

We recommend that HUD reassess the adequacy of its Atlanta and New York area offices' performance in following prescribed procedures for ensuring that all prospective developers' proposals are promptly and adequately evaluated and that the basis for selection is fully documented. Specific attention should be given to requiring the Atlanta office to make careful and timely preliminary evaluations of proposals, and the New York office to (1) rank prospective developers prior to making selections, (2) retain files on proposals for the full 3 years required by HUD regulations, and (3) ensure that procedures regarding site control are adhered to.

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We would appreciate being advised of any corrective actions taken on the matters discussed in this report.

Sincerely yours,



Richard J. Woods
Associate Director

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